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AUTHOR Minter, W. John
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ABSTRACT

Important issues and technical problems related to assessing the financial health of colleges and universities are described, along with implications of financial health assessment for state policy-making. It is proposed that a distinction be made between the assessments of financial health and program success. Other issues that should be addressed are as follows: the risks faced by institutions that seem viable; whether the financial assessment is to involve aggregate institution or individual institution data; the need to consider public and private institutions separately; and whether the assessment will be long- or short-run. The main and most persistent technical problem for financial assessment of institutions is obtaining relevant and reliable financial data. Information is needed on the impact of law suits and government regulations, the stability of revenues, the expenditure of current income for capital renewal and replacement, the institution's credit line, and its ability to handle debt service costs and to cover current liabilities in the short-run with cash and near cash. Research questions for the future may include: When is financial stress no longer a management problem but a public issue? When and how does public policy affect institutional financial health unequally so as to threaten financial distress? How can the uncertainty or certainty of revenues be identified and measured? What is the long-run capital funding outlook for higher education? (SW)

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PAPERS IN EDUCATION FINANCE

Paper No. 4

THE FINANCIAL ASSESSMENT OF
COLLEGES AND UNIVERSITIES AND
ITS IMPLICATION FOR STATE POLICY

W. John Minter
John Minter Associates

Presented at the
Postsecondary Education Finance Conference
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SUITE 300, 1860 LINCOLN STREET
DENVER, COLORADO 80295

(303) 861-4917

This paper has three principal objectives; to describe important issues and technical problems related to assessing the financial health of colleges and universities, to describe likely implications of financial health assessment for state policymaking, and to suggest some avenues for research that might profitably be undertaken in the immediate future.

Financial Assessment Efforts

Since the early 1970s, several efforts have been made to assess the financial condition of colleges and universities, public and private, to determine whether they were suffering financial distress. First it was William Jellema in From Red to Black (1971) reporting a financial crisis of grave proportions based primarily on the observations of operating deficits in current funds. The data were obtained from self-administered questionnaires returned by about 500 institutions.

At about the same time, Hans Jenny and Richard Wynn began a series of installments reporting investigations of financial health of 48 four-year liberal arts colleges. First, in The Golden Years they documented what we now refer to as the "boom years" of higher education. Enrollments were growing. Buildings were being added by many institutions. Salaries were beginning to reach acceptable levels. But towards the end of the 1960-68 period, Jenny and Wynn detected what they considered to be signs of financial distress; slower growth and more deficits. (Some deficits are reported in any period.)

Then followed The Turning Point showing that for these 48 colleges, declining enrollments, accelerating expenditures, and uncertain revenues had ended the golden years abruptly in a splash of red ink.

Richard Wynn writing in, At the Crossroads, continued the installments warning about the impact of inflation on educational program quality. All of these studies were based on a very careful analysis of institutional financial records and other related data.

In 1974, Howard Bowen under the auspices of the American Association of Colleges, launched a Study of the Financial and Educational Trends in Private Higher Education. This effort now known as the Bowen/Minter Reports, was intended to bring together in one place financial and nonfinancial indicators of financial health based on a national stratified random sample of four-year institutions. Our intent is not to peg institutions as being in financial distress, but rather to observe their financial positions and progress. Thereby providing the industry with norms by which individual institutions could judge their own financial health.

Out of this activity has grown similar continuing studies in seven states and three major associations of church-related colleges.

The limiting factor of all of these studies is the fact that they focus exclusively on the independent sector of higher education.

The Carnegie Commission in 1970 under the leadership of Earl Cheit, looked at 41 public and private institutions. Based on in-depth campus interviews, financial distress was described primarily in terms of diverging income and revenue streams. Remedies were to be found in cutting costs which may lead to deteriorating program quality. Cheit coined the phrase "the new depression in higher education," the title of the study. In a follow-up two years later, Cheit was lead to conclude that the institutions indeed had responded to financial stress and had managed to achieve a fragile stability. In this study a new measure was added to the art of financial assessment, the assumption that

any income growth rate lower than 2.5 percent above the consumer price index would lead to financial trouble.

In 1973, the Commission on the Finance of Postsecondary Education made an attempt at institutional financial assessment. Their effort was up-dated a few years later by Lanier and Anderson at the American Council on Education. The income-cost squeeze was again the focus of attention with the added concern about the effect of growing inflation.

In the fall of 1976, Change Magazine published the Andrew Lupton study. Using the technique of discriminate analysis and the Higher Education General Information Survey (HEGIS) current fund financial reports, Lupton and his colleagues concluded that at least 50 percent of colleges and universities were in or headed for financial difficulty.

All of these studies have been helpful in some way. Jellema got the ball rolling for the private sector and highlighted the existence of a serious problem. The Carnegie Commission expanded our focus of concern to the public sector. Cheit further discovered that institutions could and would respond in a positive way to financial stress. Jenny and Wynn have been among the most creative investigators with their financial distress serials. They have moved from income-cost related issues to problems of capital financing in the long-run and most recently bringing attention to the impact of inflation on the financial health of institutions. But even their studies, up through Crossroads did not consider in any detail the relationship between debt and assets. The Commission on the Finance of Postsecondary Education reached no conclusion about a standard for financial distress that could be used by an institution or a financial analyst. Lanier and Anderson updated the Commission's work and extended Wynn's inflation concepts to a broader sample of the industry. The Change article ignited considerable interest in the problem but shed little,

if any, new light into the murky corners of financial assessment. Any contribution of the Bowen/Minter study to the art of financial assessment is better undertaken by someone other than the author.

It is puzzling that after all of these studies over a period of more than five years we have not achieved any significant consensus on the art of financial assessment nor on standards of financial health. There are a number of reasons why I think this is so and I would like to describe them to you now.

Issues Related to Financial Assessment

Program or financial assessment? One of the first issues that needs to be clarified, in my opinion, is the distinction between assessment concerned with the continuing existence of a financially viable business and assessment concerned with changes in program quality which may or may not have been brought about by financial distress. Most of the literature on financial distress, particularly Cheit's work and even our own, tends to blur these two perspectives. For the educator or policymaker who seeks constantly to upgrade research and instructional programs in higher education, the relationship between financial health and program success is important. But for the financial analyst it does not necessarily follow that programs will suffer if the institution does not receive all the funds it expects. At a particular point, the notion of program quality is an important one if the analyst is concerned whether a market exists for institutional services or whether a major change in quality of service will destroy the market. It can be said, however, that in this country we have always had a wide range of quality among and within our colleges and universities. I have yet to hear one college officer say that his program is inferior because revenues failed to keep pace with expenditures or that total revenues did not equal the

original request. Colleges can and do adjust their ambitions to live within their means. So for our purposes of financial assessment I would prefer that we separate the quality issue from the financial distress issue. One can of worms is quite enough for the moment.

Bankruptcy or going-concern analysis? Another issue that should be addressed is the analyst's perspective on the life-chances of an institution or the industry. Bankruptcy and crisis analysis of this kind attracts headlines but casts little light on the problem of financial assessment for institutions that are in good shape. The latter needs some perspective on the vital signs for institutions who clearly are going to continue for some time. The latter kind of assessment we will call "going-concern" analysis. From this perspective we assume that the institution will continue to operate rather than face liquidation. The question is, what are the risks to continuing as a going-concern? The data are examined to discover whether such risks are increasing or diminishing.

Institution or industry assessment? Another issue the analyst must deal with is whether the financial assessment is to be made of an institution or the industry. I do not see any responsible way to talk about the financial health of the industry without beginning at the institutional level. Institutions suffer financial stress individually, not in the aggregate. Our data clearly show that certain types of institutions are more prone to such distress than others. Aggregate statistics often conceal such important differences. However, policymakers find it easier and perhaps necessary to deal with industry-wide problems rather than individual institutions. Aggregating institutions moves the problem into the abstract thus giving the political bargainers more elbowroom.

State or independent ownership? The issue of ownership is related to the issue of industry description, but deserves special consideration. It seems to me artificial and misleading to lump state-owned and independently-owned institutions into the same group for financial assessment. In the final analysis, state-owned colleges or universities will not go out of business unless the state collapses. Branch campuses may be trimmed or even cut off, but the corporate entity will live. Questioning the financial integrity of the state-owned institution is questioning the financial integrity of the state. No one is prepared to take that one on.

On the other hand, independently-owned institutions can and do go out of business. The manager of an independently-owned college must not only be concerned with maintaining educational quality but must also take care for the financial stability of his institution in the long-run. Whereas managers of state-owned institutions may leave the long-range financing problems to the central office, the coordinating agency, or to the executive and legislative branches of government.

Short- or long-run assessment? Credible financial assessment must move beyond the preoccupation with deficits and income-cost ratios. To look only at current operations and ignore the cumulative impact of deficits financed either by borrowing or spending one's own capital is to leave the task of financial assessment incomplete.

Three basic questions. Hans Jenny has stated the framework for financial assessment in three simple questions:

How much did we take in?

How much did we spend?

Were both revenues and expenditures adequate?

I would suggest only minor refinements:

How much did we take in and are the sources likely to continue?

How much did we spend and are there signs of uncontrolled expenditure?

Were income and expenditures both adequate to keep us in business in the long-run?

If we are able to answer these questions adequately the problems of data and financial indicators will have been resolved.

Technical Problems of Financial Assessment

Now lets turn our attention to some important technical problems of financial assessment in higher education.

Credible financial data. The principle and most persistent technical problem for financial assessment of institutions is obtaining relevant and reliable financial data. By relevant I mean numbers that reflect financial facts which tell us something real about the financial condition of the organization. By reliable, I mean the numbers actually contained the information we believe they do and the numbers for each financial period under consideration contain the same information. Fundamental concepts. Widely acclaimed but seldom achieved. Here is an example to give you some feeling for the extent of the problem.

The Bowen/Minter Reports, after the first edition, have relied exclusively on data from audited financial statements coded to the National Association of College and University Business Officers (NACUBO) standards with the result confirmed by participating institutions. Why do we go to such lengths when EDSTAT files are so easily obtainable? We have compared the HEGIS financial data with our data obtained from the audits and confirmed by the institutions. I can assure you that at the institutional level, at least, the reliability

rate of HEGIS financial reports is very low. Consider that the HEGIS financial report asks for data defined by AICPA and NACUBO guidelines. Yet in a national sample of 100 institutions only two colleges in 1975 completed the report with 100 percent reliability. The reliability of HEGIS data varies widely depending upon the section of the report and the level of dollar aggregation. Among the least reliable numbers we have found were those in the sections reporting government revenues, plant values, and endowment investment values. The most reliable numbers seem to be those for tuition and fee revenues.

The problem of reliability will not be solved by harassing the National Center for Education Statistics (NCES) or NACUBO. The problem is inherent in our diverse system of higher education. We have examined approximately 3,500 audit years of 700 colleges and universities. Our finding is that about 30 percent of the institutions are using the most recent audit guidelines as defined in College and University Business Administration, Chapter 5, "Fundamental Concepts of Financial Accounting and Reporting." Another 50 percent are using the AICPA guidelines as first published in 1973 before the Chapter 5 revisions were introduced. And 20 percent are doing their own thing. The guidelines are not mandatory. Even among the 30 percent of institutions who are using the appropriate guidelines, formats and details of the financial statements vary widely, depending upon the audience the institution is addressing; trustees, donors or creditors. In some cases the institution auditors insist on following unique guidelines unrelated to AICPA framework. Such anomalies are perfectly admissible by the guidelines in a number of instances.

From 1974 to 1976 we saw greater clarity in financial statements as colleges and universities began to implement the NACUBO guidelines. But thus

far in 1977, we have not seen a similar level of improvement. Will there be only a few who do change to the new guidelines? Audit changes do cost money. Are institutions postponing expenditures in this area to cover more urgent needs? We do not know. Our conclusion is that the only way to assure reliability in data for financial assessment is to control compliance. That is, code the data ourselves beginning with the audited statements and supporting schedules.

There are a number of other reasons why data supplied by the institution on questionnaires, particularly the HEGIS survey, are unreliable. The same person seldom fills out the HEGIS report two years in a row. In several instances the financial questionnaires are completed by the institutional research office without reference to the financial officer. The task is often handed to some clerk in this office who may not understand either the questionnaire or the institution's financial statements. Another common error we have discovered is that institutions adopt the new HEGIS terminology but continue using their old definitions. Thus Academic Support includes only libraries and not the academic dean's office and academic computing costs. Public Service often includes instructional activity as well as noninstitutional public services. Usually HEGIS information is supplied before the close of the fiscal year when accounts are finally justified. If audit changes are made in a particular year previous years of HEGIS remain unchanged thus throwing trend data completely out of line. It is often argued that errors in the HEGIS data or other survey data are washed out in aggregate statistics. That may be the case. We have no evidence to my knowledge that it is or it isn't. However, if we accept the thesis that reliable financial assessment must begin with the institution then institutional data must be reliable and accepted by the institution. It is difficult for HEGIS data to pass that test.

Relevant Data

If we solve the problem of reliable data we are still confronted with the problem of relevant data. We need facts that will help us answer the three basic questions referred to earlier. Many of these facts are not to be found in institutional financial statements. Financial facts are only part of the picture. In my opinion the auditor's going-concern concept is the most useful criteria for sorting out the facts that we need for relevant financial assessment.

The first set of facts are nonfinancial but given negative trends in these facts there can be serious financial consequences. Take for example the fact of staff morale. When everyone pulls together and is enthusiastic about what is happening the institution is successful. On the other hand if staff are discouraged, at cross purposes or unhappy for any reason, institutional success begins to slip away. The whole tone can be affected by staff morale. When it is high, energy, resources and good will seem to flow to the organization. When morale is low, the level of energy, resources and good will begins to diminish. These facts appear only between the lines in financial statements. They can be inferred from student attrition data, from faculty turnover data, but not with great reliability. These facts are usually obtained in confidential interviews.

Litigation. The income and expenditure pattern of a college can be seriously affected by law suits and by rulings by government agencies. Such information may appear in the financial statement. Usually it does not. These facts are most reliably obtained from the executive officer and legal counsel.

Stable revenues. Critical to the continuing financial success of any organization are its revenues. Much of our attention is now focused on the relationship between revenues and expenditures that is entirely appropriate

in the short-run period. In the long-run, however, we must also be concerned with the quality of revenue sources; with their stability. One set of facts about revenues, distribution ratios, tells us of changing proportions of revenues among the principal sources. A study of the changing dependencies among revenues will perhaps give some clue to revenue stability. Another set of facts, percentage change over time, tells us whether the flow of funds from revenue sources is increasing or decreasing. For example, revenue from tuition and fees has recently been increasing as well as the proportion of total revenues and the percentage change over time. That may look good. But increased dependency on tuition and fee revenues must take into account the impending drop in college-age population; changing patterns of learning beyond high school, and competition with new learning patterns offered by other institutions. Or consider revenues that are based on government research and development priorities or revenues that depend on dividends in the stock market. The quality and stability of these revenues can be assessed only with facts about the demographic and economic environments which generate their flow. It would not be true to say that all institutions ignore these kinds of data. But when one looks at enrollment projections it is curious that almost no institution, state or independently owned is projecting a down-turn in enrollments. As one president told me, our admissions office believes we can beat it. Such facts about revenue stability in the long-run are crucial to the financial assessment of colleges and universities.

Expenditure control. Equally critical to the institution is making sure, in the long-run, that revenues cover an adequate level of expenditures. Whether or not operations are sufficiently funded and balanced in the long-run is difficult to determine for an individual institution and particularly for

the industry. First of all, fund accounting principals make it very difficult to calculate a "bottom line." The bottom line can be calculated at any one of three points in a current fund statement; after total expenditures but before mandatory transfers, after total expenditures and mandatory transfers, or after all expenditures and transfers. In addition, 10-15 percent of expenditures may be incurred in other funds, never reported on the current fund statement and thus escape our calculations.

In general, expenditures are out of control or balance when they exceed revenues over time or their rate of increase exceeds the rate of increase for revenues. We say, "in general," because an institution may deliberately run deficits to finance activity calculated to improve the institution's position in some manner with an assumption that in the future larger revenues will bring the two in balance.

Richard Wynn and Hans Jenny have called our attention to important costs seldom considered but nonetheless, justifiable deductions from revenue; these are inflation, which escalates the cost of doing business with no gains in quality or productivity, and the impact of obsolescence and wear on institutions that depletes capital investment which sooner or later must be replaced at ever spiraling costs.

The expenditure of current income for capital renewal and replacement is a policy followed by few institutions. The fragile stability described in our studies of the private sector would probably disappear if true capital costs were being included in the regular budget. Typically, colleges defer such expenditures to the capital funds campaign in the hope that past sins of omission will be covered by the grace of generous donors.

The second set of important facts about a going-concern have to do with genuine financial matters. The first important fact that seldom if ever

appears on published financial statements is the institution's credit line. Successful financial strategy may require bank loans or capital acquired through the sale of bonds. An early warning of financial distress may be the failure to qualify bond issues or obtain a bank loan at favorable interest rates, if at all. Facts about the institution's credit line are confidential and not included in current surveys. The chief financial officer or principal creditors are the most reliable sources for this information.

Default. Another important fact that seldom appears in published financial documents is the report of failure to meet debt obligations or the renegotiations of loan covenants more favorable to the institution. The reason some institutions can continue with very low or negative current fund balance or very low equity ratios and current ratios is that creditors have been willing to postpone collections or write off bad debts to keep the enterprise alive. If the economy really hits rough going or for some other reason creditor good will is lost, the colleges with high risk in this area will experience severe financial distress, if not closure.

Equity. Originally, our use of financial statements was prompted by a desire to capture the complete picture of financial condition. Financial assessment simply cannot be taken seriously without reference to facts about debt and net worth. Financial statements do report fund balances which make up the net worth or equity of the institution (total assets minus total liabilities). It is the relationship between liabilities and assets that informs us about risks to the going-concern. Going out of business or "what can we do to save the ship" analyses, would, of course, focus on expendable assets and in particularly expendable net worth. Table 1 shows a gradual improvement in liability coverage over the past three years for a national

TABLE 1

STATISTICAL SUMMARY OF TOTAL ASSET COVERAGE OF TOTAL LIABILITIES

(Asset/Liability Ratio)
95 Independent Colleges and Universities, 1974 to 1976

<u>Ratios Distribution</u>	<u>1974</u>	<u>1975</u>	<u>1976</u>
Minimums	1.4:1	1.7:1	1.7:1
25th Percentile	3.3:1	3.3:1	3.3:1
50th Percentile	4.2:1	4.5:1	4.7:1
75th Percentile	6.2:1	7.2:1	7.4:1
Maximum	52.6:1	40:1	37.5:1
Aggregate Dollars	4.5:1	4.6:1	4.6:1

sample of independent colleges and universities. However, the maximum ratio has been declining steadily suggesting that well-endowed institutions are using up reserves without replacement. Table 2 compares the asset/liability ratio of Carnegie Liberal Arts I Colleges with Liberal Arts II. The contrast between well-endowed and not so well-endowed colleges is readily visible. That is not to say that the latter are more vulnerable to outside economic forces, they are vulnerable to a different set of forces. The small liberal arts college also have less margin for weathering economic drought. Hence they are, indeed, higher risk institutions from the purely financial point of view.

An important and related financial fact is the institution's ability to handle debt service costs. The analyst asks to what degree will total revenues cover principal and interest payments? Table 3 shows such a ratio for the national sample of independent colleges and universities. The position of universities and liberal arts colleges is superior to the other types of institutions. However, all but the comprehensive colleges have registered

TABLE 2

COMPARING ASSET/LIABILITY RATIOS FOR NATIONAL SAMPLE
LIBERAL ARTS COLLEGES I AND II, 1974 TO 1976

Ratios Distribution	1974		1975		1976	
	LAI	LAII	LAI	LAII	LAI	LAII
Minimum	3.3	1.4	3.4	1.7	3.7	1.7
25th Percentile	4.8	3.0	5.0	3.1	5.1	3.0
50th Percentile	9.0	3.6	9.2	3.6	8.9	3.6
75th Percentile	13.3	4.3	14.9	4.8	15.8	4.7
Maximum	29.1	52.6	27.5	40.0	37.5	34.4

TABLE 3

REVENUE COVERAGE OF CURRENT FUND PRINCIPLE AND INTEREST
AND INTEREST ON PHYSICAL PLANT DEBT,
NATIONAL SAMPLE OF INDEPENDENT COLLEGES AND UNIVERSITIES

	Mean Coverage		
	1974	1975	1976
All Institutions	42:1	35:1	33:1
Universities	54:1	56:1	42:1
Comprehensive Colleges	23:1	22:1	23:1
Liberal Arts I	83:1	58:1	52:1
Liberal Arts II	27:1	24:1	26:1

declines in this ratio (increasing financial risk) from 1974-76. The Liberal Arts I colleges especially are exhibiting declining financial strength in this regard.

Liquidity. One clue to the cash flow of an institution or its ability to cover current liabilities in the short-run with cash and near cash is the

current ratio (total current asset coverage of total current liabilities). Once again, the smaller, less selective liberal arts colleges are the most vulnerable from the financial point of view (Table 4). These colleges as a group have only 90 cents to cover every dollar of current liability. On the other hand, Liberal Arts II colleges seem to be in the strong position and getting stronger.

TABLE 4
CURRENT RATIOS,*
NATIONAL SAMPLE OF INDEPENDENT COLLEGES AND UNIVERSITIES
1974 to 1976

<u>Institution</u>	<u>Median Ratio</u>		
	<u>1974</u>	<u>1975</u>	<u>1976</u>
All Colleges and Universities	1.4	1.4	1.3
Universities	1.4	1.4	1.3
Comprehensive Colleges	1.5	1.4	1.5
Liberal Arts I	2.1	2.5	2.7
Liberal Arts II	.9	.9	.8

*Total current assets coverage of total current liabilities.

Another way to look at financial liquidity is to consider the availability of unrestricted funds balances. If the ratio of unrestricted funds balance is diminishing we might reasonably assume that financial flexibility is shrinking. Table 5 tells us that to some degree that is exactly what is happening to independent colleges.

To summarize, we have outlined briefly the principal types of indicators we think are essential to the financial assessment of institutions and by

TABLE 5

UNRESTRICTED FUNDS BALANCE AS A PERCENT OF TOTAL FUNDS BALANCE
NATIONAL SAMPLE OF INDEPENDENT COLLEGES AND UNIVERSITIES

Institution	Median Ratios		
	1974	1975	1976
All Institutions	7.8	7.5	7.3
Universities	9.3	7.7	7.6
Comprehensive Colleges	7.7	7.5	6.9
Liberal Arts I	10.6	10.4	10.1
Liberal Arts II	3.7	3.6	3.4

inference of the industry. Some of these facts can be found in financial statements, many cannot. We have illustrated a few facts from the balance sheets of colleges and universities because this aspect of the financial picture has not been widely used up to this time. These particular facts are most useful in getting some feel for the impact of current operations on the long-run financial well being of the institution. Without them there is no way to evaluate the impact annual fluctuations in current revenues and expenditures especially when the institution appears to be operating with deficits. More experience is needed in drawing inferences from these trends and in relating them to nonfinancial facts of the going-concern.

Implications of Financial Assessment for State Policy

What meaning do these facts have for state policy? Perhaps we should be more specific. How will the financial assessment of colleges and universities serve to direct more funds to higher education? Based on my observation of several state associations of independent colleges and universities and their use of financial assessment data, the answer will be, indirectly and with considerable variation from state to state.

Such an answer is consistent with the findings by Lyman Glenny and his colleagues at the Center for Research and Development in Higher Education at Berkeley, California. The Center has recently published a series of books titled State Budgeting for Higher Education. (See annotation in the bibliography.) The research these men have completed is comprehensive, thorough, and draws upon important literature in the fields of political science, public policy and public administration. Their integration of these fields with research findings in higher education budgeting are provocative and enlightening. While describing the advances made in application of computerized information systems and new analytical techniques, In the Political Economy of the Process, Schmidtlein and Glenny reach the conclusion that greater awareness is needed of the limits of technical analysis as a means to reduce controversy in budget decisions. The authors maintain that in a democratic society technical analysis cannot answer the question of how monies should be appropriated but only inform the bargaining process by which such issues of personal preference are negotiated in the political arena (Schmidtlein and Glenny, 1977). Glenny goes on to assert in Interagency Conflict and Consensus (after looking at the budgeting process in 17 states) that "political reality shapes the decisions to a far greater extent than systems rationales based on "scientific" or market conceptions (1976). In what could be considered a more limited context, the authors did determine that extensive information systems were useful in planning specific budget cuts required by general budget reductions. The policy decision to cut expenditures had already been made (Bowen and Glenny, 1976).

The technical and political consequences of using information systems is discussed by Purves and Glenny (1976), in Information Systems and Technical Analyses.

Following their list of benefits and problems here are some parallels related to information about financial assessment.

Possible benefits. Because the issue of financial health has been considered and the discussion supported by relevant and (hopefully) reliable information, final decisions are more likely to be equitable or at least perceived so by the bargaining parties. The principal difficulty in achieving this benefit may well be developing financial assessment techniques that are perceived to be credible by both state and independently owned institutions.

Second, with improved financial assessment the dialogue will no longer be over the fact of financial health but will now focus on the relative merits of courses of action that should be taken if the sector of the industry appears to be in serious financial difficulty.

Third, the process of financial assessment itself may bring about desirable changes at the institutional level. Indeed, such changes have been reported in states where our financial series are being used.

Possible difficulties. No matter what they are, the final results of financial assessment, either of an institution or of the industry, will not please everyone. The facts will not fit every political bargaining situation. Arguments may be deflated or the integrity of the advocates may be brought into a question. I agree totally with Purvis and Glenny (1976, p. 143) when they conclude:

"Participants are more likely to seek and use data which suit their preferences than to alter their behavior as a consequence of information availability."

Financial data will always be under attack for noncomparability particularly by those who disagree with its implications. No matter how hard we work to control compliance with standard definitions there will always be loose ends.

By their very nature higher education institutions vary widely right down to the last level of detail. Even recoding of every transaction would fail to achieve absolute comparability. We have discovered another technical problem mentioned by Purvis and Glenny; that some institutions simply cannot provide the financial data under any circumstances. They do not know. The questions have never been asked.

Another set of problems relate to the non-use of data. HEGIS financial data has long been the target of criticism that it is always late and irrelevant to the issues. No set of financial assessment data will entirely be free from such accusations. Specific policy issues will always require specific studies. One answer to the problem is to control compliance as we do by coding documents to meet a common standard and to do so with a sample of institutions which makes a short turn around time reasonable. In the financial area and in the private sector this is possible because national standards have been adopted by the industry. In addition, the private sector has a strong felt need to develop credible financial assessment data.

Purvis and Glenny also discuss the misuse of data as a potential problem. They conclude, I believe correctly, that there is no way to protect ultimately against incorrect inferences or comparisons. Users will continue to draw inferences and make comparisons they prefer while blithely ignoring the caveats we analysts so carefully weave among our conclusions.

Finally, institutional financial assessment data will take its place beside every other kind of data used by advocates to advance the interests of their constituencies in the political arena. If the information is seen to enhance the case it will be used. If not, it will be soft-pedaled, ignored or even denied. Does that mean financial assessment is a waste of time or a trivial exercise? Not at all. Every serious step to improve the quality and

reliability of financial data will lead toward better understanding of financial health by administrators and trustees at the campus level. Institutional financial success or failure is, after all, largely in the hands of these people.

TOPICS FOR FURTHER RESEARCH

During the past eight years or so, we have learned a few things about institutional financial health: How difficult it is to define and measure; how difficult it is to just get reliable facts; how difficult it is to achieve consensus on what analysis of financial facts mean. Some of us have even ventured to describe the financial trends of the industry while still seeking a better understanding of the economics of educational firms. Much remains to be observed and understood. The following questions come to my mind as I puzzle over financial data and attempt to make sense of the patterns found there. "

Colleges have been a part of the institutional landscape almost from the beginning of this country. Many, but not all, have survived. The survivors can all testify to periods of financial stress. But only in this decade has there seemed to be a preoccupation with the financial health of the industry? Jellema foresaw a major disaster if trends continued. Lupton believed at least half the institutions were in or headed for financial difficulty. The other major studies arrive at a broad consensus of 25 percent to 35 percent of the industry experiencing financial stress at any one time. But whose problem is it? When is financial stress no longer a management problem but a public issue?

Related to this question is the important distinction to be made between financial distress caused by poor institutional management and distress

resulting from poor public policy. At what points and in what ways do public policies unequally impact institutional financial health so as to threaten financial distress? As a voter and taxpayer I am concerned about the distress caused by my elected representatives but I am not especially interested in bailing out inept management.

Each of the studies of financial health has stated or implied a set of financial indicators. Yet we have little concrete evidence over time and over a large number of institutions that our numbers connect to financial reality. What are the most reliable and sensitive indicators of a college or university as a going concern?

Most analyses of financial health focus on financial statements or reports because they are available. But the causes of change in financial health are not to be found there. If we are expecting public policy to provide fast, fast relief we need to gain a broader understanding of the causes of distress. For example, at what points and how does staff morale affect the financial conditions of an institution?

At what points and how does litigation typically affect the financial condition of an institution?

How can we identify and measure the uncertainty or certainty of revenues?

How can we identify and measure expenditure control or lack thereof?

Institutions are not islands. So we must also ask at what points and in what ways do changes in general economic conditions threaten financial distress for the institution? Revenue stability and expenditure control presumably are closely linked to the national economy.

Two types of financial facts are not readily available but usually can be obtained if one "needs to know." These are facts about credit ratings and

defaults on loan obligations. Such information developed by banks and creditors should be among the most reliable and sensitive measures of financial condition. What are the credit rating patterns in higher education and how are they changing? Are colleges and universities increasingly defaulting on debt obligations or can they manage their debt service without stress? We simply do not have any comprehensive or reliable information about these issues.

One of the ways in which the financial strength of industries are measured is the degree to which capital stock is increasing or decreasing. If capital is eroded through either direct expenditure or through failure to charge current revenues for renewal and replacement, in the long run the firm will be out of business. Many colleges and universities are gambling deferred capital expenditures against future gifts.

What is the long-run capital funding outlook for colleges and universities and its implications for current and future financial health? What are adequate levels of revenues and expenditures for higher education in the long-run?

While much attention has been paid to the financial health of independent colleges, state institutions have been subject to similar financial pressures. It is likely that state financial policy issues will require assessment of both. Is it possible and desirable to compare the financial health of state-owned and independently owned colleges and universities?

Not all institutions are suffering financial stress. And the 25 percent to 35 percent who do are not the same institutions from year to year. We are being asked more often what are institutions doing who cope successfully with financial stress? How have they changed? How has their environment changed?

The result of institutional change brought about by financial stress is often viewed as negative. On the other hand, a little stress may induce

necessary changes that prevent future disaster. Institutions have been known to provide superb instruction, even in bankruptcy. It is important to know at what points and in what ways financial distress seriously affects educational quality. In the short-run financial stress may have a beneficial effect. But over time, continued, inadequate financing can only erode educational quality.

The fundamental question remains; are American colleges and universities gaining or losing financial strength? Only partial answer can be given with available data. Certainly the industry as a whole is not growing at the rapid pace of the sixties. Based on available data, the independent sector is holding a fragile balance. We have no comparable data for the state sector. If, however, the impact of inflation is considered and adequate changes are made for capital replacement and renewal, the fragile balance is destroyed. Only those institutions with substantial reserves either in tangible assets or political support may weather the stress with programs intact.

Of all these questions that might be researched, top priority should be given to determining what are adequate levels of revenues and expenditures for quality higher education programs in the long-run? The first task will be to establish a range of acceptable costs for quality programs by field, level and target participants. Some of the work undertaken by NCHEMS may be providing this necessary base-line. We are not concerned only about operating costs but capital costs as well including the cost of capital replacement and renewal. The next task will be to bring together the data on trends that will change base-line costs over time. Projected levels and changing patterns of economic growth along with inflation trends will be one key component. Demographic trends in relation to changing patterns in college attendance will

be a second key element. Trends in the knowledge industry itself; new fields, new applications and new modes of teaching/learning activity will need to be considered. The objective ought not to be to develop one trend line but several, each based on a different scenario. The results of such a study would provide useful long-range financial guidelines to state legislatures and congress.

ANNOTATED BIBLIOGRAPHY

Adams, Walter. "Economic Problems Confronting Higher Education: Financing Public Higher Education." The American Economic Review, 67:1, pp. 86-9, February 1977.

The current recession in public higher education is a secular not a cyclical phenomenon and may be due to the following diagnoses:

1. Demand projections for higher education are as naive as exponential population forecasts, e.g., incorrect estimates of need for scientists and engineers, incorrect estimates of increases in student populations.
2. The demand for higher education, especially public, has both a "natural" and an "artificial" component, e.g., autonomous market forces vs. derived demand, levels of state and federal support, choices of natural priorities such as space exploration.
3. State appropriations for higher education have shown a long-term increase, but appropriations are unduly influenced by cyclical fluctuations of the economy, e.g., budget policies in some states are influenced by the business cycle. Stabilization funds are needed.
4. The half-hearted commitment of the federal government to higher education and current methods of financing by the states, tend to undermine a central function of public higher education, viz to serve as an instrument of vertical mobility in a democratic society -- this is especially so in periods of rapidly rising prices for tuition and auxiliary services (Michigan is cited as an example).

The fault lies in our values and priorities.

Astin, Alexander W. "On the Failures of Educational Policy." Change, 9:9, pp. 40-3, September 1977.

The main objectives behind the expansion of our higher education system during the sixties and seventies were purely political: Access and supply manpower to areas of political interest. Cutting operating costs is now the political objective. Thus, the neglect of the putative ideal of higher education. A national survey found that policy changes have not only failed to enhance programs but have contributed to their deterioration: policies such as massive expansion in the public sector, large institutions, eclipse of single sex colleges, proliferation of community colleges, de-emphasis of dorm living, increased dependence on loans for financial aid, and open admissions.

Notable is his opinion that the shift towards larger institutions has fostered student liberalism, business interests, hedonism and religious and political apostasy. Altruism and intellectual self-esteem are promoted by the smaller colleges. The author stresses the beneficial aspects of grants and work-study programs, yet policymakers opt for financial aid presumably because it is less expensive. The author is particularly concerned with the trend toward watered down educational programs due to policymakers viewing resource allocation as an end in itself.

Bailey, J. J. and R. J. O'Connor. "Operationalizing Incrementalism: Measuring the Muddles." Public Administration Review, 35:1, pp. 60-6, January/February 1975.

Incrementalism has been employed as a general concept to describe policymaking, but several difficulties have arisen in its application to budgeting. Specifically, analysts have not distinguished between bargaining processes and incremental results or outputs (i.e., small changes from a given base). Rather, it is assumed that bargaining processes

necessarily produce incremental outputs. This assumption in turn has created a second difficulty: the lack of specific criteria to distinguish incremental from nonincremental outputs. The work of several authors is examined to illustrate the logical and analytical problems encountered when the distinction between process and output is not observed. Generally, scholars have slighted data in their own work indicating evidence of nonincremental outputs. Illustrative budgetary data are provided to demonstrate the incidence of apparently nonincremental budgetary outputs and the obvious need to refine further the concept for empirical research.

Balutis, A. P. and D. K. Butler. Editors. Political Pursestrings: The Role of the Legislature in the Budgetary Process. New York: Halsted Press, 1975.

This is an examination of the state legislative role in the budgetary process. Seven states are reviewed in depth: New Mexico, Florida, Michigan, Illinois, Wisconsin, New York and Texas. The roles of the legislative staff can be summarized as,

- (a) implementing the rational comprehensive method by supplying, organizing, and presenting neutral, minor and technical information;
- (b) implementing the rational comprehensive method by creating and criticizing proposed policies, often in a biased manner; and
- (c) implementing the successive limited comparison method by rationalizing compromises and bringing interested parties together" (Morley Segal).

State budgetary processes are a generic prototype of the policymaking process. Roles of the legislative staffs are divided into intelligence, integration, innovation and influence.

In sum, the following are avenues for relevant research: (1) differences between staff members in background, recruitment, career aspirations, norms and functions; (2) different types of staff have different types of tasks and desired affects; (3) staff may be more

likely to reinforce existing opinions of legislators than to change such opinions; (4) nature of complexity; (5) staff influence increases as the legislation under consideration becomes less political, less controversial, or less partisan; (6) affect of images; (7) explicit conclusions or recommendations from staff are more influential than a report which allows legislators to reach their own conclusion; (8) staffs are as influential as the legislator; (9) legislators under cross-pressures are more susceptible to staff influence; and (10) staff influence is related to legislator's perception of his/her role and career outlook.

Bowen, Frank M. and Lyman A. Glenny. State Budgeting for Higher Education: State Fiscal Stringency and Public Higher Education. Berkeley: Center for Research and Development in Higher Education, University of California, 1976.

Five case studies of procedures used in reducing expenditures for higher education at the state level. Descriptive and prescriptive.

Retrenchment is unfortunate even if unavoidable. It can cause personal tragedy, and it inevitably entails institutional disruption and trauma. It can drastically alter an entire educational system, as it has in the City University of New York. It may result in continuing lower funding levels with a similarly drastic impact on individual programs or departments. It may reduce educational opportunities by limiting enrollment or imposing higher tuition. But adversity has its uses. Those who have experienced retrenchment are now fully aware that institutional vitality depends on the willingness and ability of faculty and administrators to state specific academic program objectives, to order these as priorities, and to allocate resources accordingly. They are also aware that the task requires the informed cooperation of executive and legislative fiscal agencies.

Bowen, William G. "Economic Problems Confronting Higher Education: An Institutional Perspective." The American Economic Review, 67:1, pp. 96-100, February 1977.

Some simple concepts can improve understanding of why resources are not meeting needs:

1. "The instinct of survival" keeps institutions from closing in the face of financial difficulties. However, this instinct sometimes fails to meet reasonable criteria of effectiveness. The danger is slow but cumulative decline. Warnings are not heeded of measures of output that ignore qualitative considerations. Productivity is not quality oriented. Costs per student is not a viable form of analysis of worth. This is not to say that some cuts are salutary. It is one thing to accept a reasonable period of consolidation or retrenchment which has an end to it and quite another to be unable to respond positively (over time) to initiatives. Financial equilibrium needs to do more than preserve the status quo, at the sacrifice of the future.
2. Equality of opportunity and access is threatened by rising costs, given insufficient amounts of student aid. This cannot be allowed to affect human resources. (Portable graduate fellowships is discussed.)
3. "Community" and commitment to common goals is discussed as threatened by a production function within the universities. Ergo, protecting one's own vested interest is promoted during periods of financial distress.

Caplan, N., A. Morrison and R. J. Stambauh. The Use of Social Science Knowledge in Policy Decisions at the National Level. Ann Arbor: Center for Research on Utilization of Scientific Knowledge, Institute for Social Research, 1975.

This is an indepth study of the policy uses of social science research. The survey included 204 people in decision making in the executive branch of the federal government with extensive experience. Among the pertinent questions was the respondent's interest and use of social indicators and

their impact on policy formulation. The study showed that policy impact was most significant for issues affecting population segments. Sensitization of policymakers to social needs was most important, with evaluation, structuring alternative policies, implementation, justification and choice following in that order. Notable is that analysis was rated as a mediocre source of relevant data for utilization.

Carroll, Maryanne. An Adaptation of Financial Analysis to Higher Education. National Center for Higher Education Management Systems, August 1973.

This unpublished paper is a systematic effort to relate commercial business ratios to higher education institutions. The discussion is set within the context of federal decision making and does not distinguish between state and independently controlled institutions.

Change Panel on Academic Economics. Colleges and Money. New Rochelle, New York: Change Magazine, 1976.

A faculty guide to academic economics. The appearance of financial reports and budget summaries are increasingly evident at faculty committee meetings. Faculty must appreciate and understand some of the tensions between simple financial assertion and complex accounting exhibits, and between the accountability needs of auditors and the needs of managers and their consistency. Faculty needs to be involved in financial exigency.

Chartrand, R. L., K. Janda and M. Hugo. Editors. Information Support, Program Budgeting, and the Congress. New York: Spartan Books, 1968.

This is a collection of articles dealing with problems and prospects in information support for Congress, and implications for the Congress of PPBS. Particularly relevant is the discussion by R. N. Grosse (then the Deputy Assistant Secretary for Program Coordination in HEW), of the

analysis function of PPBS. Within, he reviews a number of programs and their alternatives according to financial exigency, viability, and results leading to recommendations. He also stresses the importance of social indicators often not subject to statistical evaluation, and the skepticism thereof. R. K. Fenno's discussion of the impact of PPBS on the congressional appropriations process. PPBS inevitably has political consequences and is not simply a matter of efficiency. Appropriations is legislative power. He discusses the "executive-legislative appropriations interface." However, the appropriations system also serves as a check on individual career aspirations, and he discusses the decision-making process of the subcommittee and their three sources of information: program, confidence and support. The suspicions of analysis are also discussed. W. Z. Hirsch later points out that PPBS assists decision making on three levels: selects a budget mix across large programs; determines best mix of sub-programs; and allows low-level decisions concerned with inputs (trade-offs). P. Szanton summarizes with a plan for more sophisticated methodology for analysis.

Cheit, Earl F. The New Depression in Higher Education. Carnegie Commission on Higher Education. New York: McGraw-Hill Book Co., 1971.

The growing financial problems in higher education and the desire of college presidents and other administrators to learn more about how individual institutions are coping with them motivated the Carnegie Commission to sponsor this study. The investigation involved 41 case studies based on "on site" interview reports and appropriate financial records. The sample selected for the study represents several types of institutions: public and private, universities, liberal arts colleges, comprehensive colleges, and two-year institutions. It was found that 29

of the institutions (71 percent) either were headed for financial trouble or were already in financial difficulty. An institution was considered to be headed for financial trouble if, at the time of the study, it had been able to meet current responsibilities but could neither ensure that it could much longer sustain current program and quality standards nor plan to support evolving program growth. Colleges and universities forced to reduce services or eliminate important educational programs were considered in financial difficulty.

On a nationally weighted basis, the institutions discovered to be heading for financial trouble represented 42 percent of U.S. institutions (1,000) accounting for 54 percent of the students. Again on a weighted basis, slightly less than one-fifth, or 19 percent of the institutions, accounting for 24 percent of the students, were in financial difficulty.

In addition to revealing the magnitude of the current depression in higher education, Professor Cheit calls attention to the nature and impact of the financial problems as they affect institutions of various types, and to the response being made by these institutions. The author's case-study examination of expenditure patterns, income factors, and administrative practices enables the reader to obtain a down-to-earth perspective of a variety of financial problems and how they may be most effectively solved. The study also presents views of school administrators concerning public policy toward financing higher education.

Cheit, Earl F. The New Depression in Higher Education -- Two Years Later.
New York: McGraw-Hill Book Co., 1973.

1. Response to financial difficulty: private institutions have adjusted more quickly than public, and research universities have been affected most adversely (although the most relevant to national welfare). No two are alike.

2. Expenditures per student per year (in the sample) above the general rate of inflation has decreased from 4.0 percent to 0.5 percent. The Carnegie Commission maintains that a rate of 2.5 percent can be handled without loss of quality -- a rising student/faculty ratio has helped hold down costs. Do more with less.
3. Federal legislation has not relieved the financial pressure on the colleges and universities. The realization that lobbies are needed has come from disappointment.
4. The task that colleges and universities prove their efficiency has been met, but no unifying set of purposes has been demonstrated -- outward appearances of stability.
5. All colleges designated as headed for financial trouble have cut their budgets without reducing quality to date.
6. The fragile character of stability is discussed (reductions made cannot be sustained).

Institutional change must accompany economic stability.

Cheit, Earl F. "The Management Systems Challenge: How to be Academic Though Systematic." In J. F. Huges (Ed.), Education and the State. Washington, D.C.: American Council on Education, pp. 147-73, 1975.

Systems analysis is relatively new for higher education. The systems approach involves the use of techniques, a framework to help decision-makers choose. Management systems include the analytical tools, the techniques for widespread use, and the conception of organization as process. Is it effective? Change and innovation are taking place but success cannot be evaluated for some time. He refers to The New Depression in Higher Education -- Two Years Later, for confirmation. Efficiency and

inefficiency concepts do influence attitudes toward higher education. Congress persons are quoted to confirm. Will management systems accelerate the trend toward centralization of higher education? The example of NCHEMS is used. Will the use of management systems reduce diversity on higher education? Only if academic goals are neglected. Do systems requirements themselves tend to influence decisions about education? That is a matter of conjecture and concern. Can colleges and universities be academic though systematic? Management systems are tools but not neutral. As a result of systems, the power of the formal structure is increasing. The key is the quality of academic leadership.

Clifford, Donald K., Jr. "Thriving in a Recession." Harvard Business Review, 55:4, July-August 1977.

A new study of corporate performance shows that in the problem period of 1974 and 1975 some "threshold" companies, by drawing on their inherent advantages of flexibility and responsiveness, outperformed their giant competitors. This article shows that lessons can be learned from these companies' experiences, and the author describes the common pattern found in the strategies and management of the successful corporations.

Collier, Douglas J. The Analysis of Institutional Financial Health: A Workshop Report. National Center for Higher Education Management Systems, October 1973.

A summary of discussion and opinion of two workshops considering the Carroll and Collier papers on financial analysis and financial distress. Development of financial ratios for higher education should be encouraged. But, the definition of financial distress escapes a resolution. Many definitions may be needed.

Collier, Douglas J. The Determination of Institutional Financial Distress: A Proposal for Decision Making. National Center for Higher Education Management Systems, August 1973.

A companion paper (unpublished) to the Carroll paper, setting some of the concerns to be addressed by financial indicators.

Glenny, Lyman A. State Budgeting for Higher Education: Interagency Conflict and Consensus. Berkeley: Center for Research and Development in Higher Education, University of California, 1976.

The complexity of the budgetary process, in which so many independent bodies sequentially or simultaneously review the higher education budgets, results in complicated interorganizational relationships and apparent overlap or duplication of roles. Despite disagreement and lack of theory, budget professionals are moving slowly and pragmatically toward a more systematic approach to budgeting.

The present study began in July 1973, when the Center for Research and Development in Higher Education undertook a three-year, 50-state study of the processes used by state agencies to formulate the budgets of colleges and universities. Its twofold purpose is to advance budgetary theory and to give state and institutional budget professionals a broader understanding of (1) the interrelationships, roles, functions, and objectives of the several state agencies in the budgetary process; (2) the congruence or incongruence of such objectives among the several agencies; and (3) the practices and procedures that build confidence in the fairness of the budgetary process.

Reports based on the study describe and analyze the organizational structures and staffing of state-level agencies and the progress of institutional budget requests through these agencies from the time that prebudget submission instructions are first issued by a state agency

until appropriations are enacted. The primary emphasis is on the budget review and analysis process and the procedures used by the state agencies; the study concentrates on the administrative interfaces among the several state agencies that review and analyze budgets and between these agencies and the institutions, or systems of institutions, of higher education.

Hoos, Ida Russakoff. Systems Analysis as a Technique for Solving Social Problems: A Realistic Overview. Working Paper #88. Berkeley: University of California, Center for Planning and Development Research, 1972.

This article is a variation on the moon and the ghetto analogy. The expertise can be transmitted if we have the wit to apply our scientific know-how to the analysis and solution of social problems with the same creativity. Why? Because of the prestigious origin and logical, scientific area of systems analysis, and the growing recognition of the need for better planning, organization and management. Systems analysis has appeal, but the relevance is at debate. Social systems are not reducible to measurable and controllable components across the board. Perspectives are manipulable. "Solutions" cannot be achieved. After much flipping of charts, progress reports and future predictions, the air is no safer to breathe. Resources must be harnessed to "produce." The community of problem solvers is more concerned with obtaining another grant than improving the state of the nation. Systems analysis is used as a political bandwagon -- regardless of their intrinsic worth! Hoos pleads for the active participation of competent behavioral scientists. Economic, political and social rationality must all play a part in developing a viable model. Creative synthesis.

Howard, S. K. Changing State Budgeting. Lexington, Kentucky: Council of State Governments, 1973.

This is a comprehensive text on budgeting, covering the full range from methodologies to underlying issues to impacts on legislature. As an art, representative politics requires compromise, and nowhere is this more apparent than in state legislatures, where a multitude of interests collide. Legislatures review budget proposals with the intent of making decisions about policies and allocations, and aim to make these decisions in a rational manner, tempered by political realities. However, control is the issue, and there is just not enough review. Permanent appropriations and earmarked funds are often not subject to legislative review. Time is also a problem. Budget appropriations are not neutral politically. Of note also is the fact that supporting documents are not reviewed, only the bills themselves. Bill drafting is the crucial stage. Revenue and expenditures are often reviewed separately. Thus, analysis itself is only part of the battle. It is not apparent that legislators will operate any differently if information comes to them in a different form. Whatever the impact rationalistic budgeting may have upon state legislatures will probably be determined by the legislatures themselves. One quote of note is, "Legislators get caught spending inordinate amounts of time trying to save relatively trifling sums." The nitty-gritty is discussed via post-auditing. Howard begins by stating its value is underemphasized. It has been used more as justification rather than constructive evaluation. Performance auditing should answer the question, "Have we met the need at a minimum cost?" But even within this text, post-auditing is still viewed as a final step-Tant pis!

Jenny, Hans R. "Higher Education Finance: Health and Distress." In J. F. Hughes and Olive Mills (Eds.), Formulating Policy in Postsecondary Education: The Search for Alternatives. Washington, D.C.: American Council on Education, 1975.

This article starts with a discussion of financial health, educational health, and accountability and a balance thereof. Sound financial balance consists of: (1) adequate financial resources; (2) the institution defining who its clients shall be and what services it shall provide; and (3) once scarce monetary resources are to be allocated, answering the question of how well the services are being performed. Although much is not measurable in higher education, it cannot be ignored. Of note is the author's statement (along NCFPE lines) that financial weakness matters only if broadly accepted public policy objectives are not being achieved. The evaluation of inflation and of the changing institutional purchasing power is summarized and generalized. Notable is his proposal that a level of how much further real per student expenditures should be allowed to drop should be determined by individual institutions. A set of credible price deflators for higher education would be a useful tool for analysis. The author also pleads for internal allocations of resources for public statistical and analytical purposes (particularly in the private institutions). Financial crisis is not new but the problem of public accountability (and accompanying respectability) must be paramount.

Magarrell, Jack. "Politics, Not Formulas, Now Cutting Budgets." The Chronicle of Higher Education, XI:2, September 22, 1975.

Retrenchments are a reality, and formula budgeting is used to analyze budget figures already arrived at through negotiations. So what is the criteria for eliminating programs. Ten items were isolated in a survey done by the Iowa Board of Regents: (1) the number of graduates from the program in the last five years; (2) enrollments and dropouts; (3) student interests and demands; (4) size and costs; (5) costs per graduate; (6) quality by reputation and position achieved by graduates; (7) improvements

achieved by consolidation or elimination; (8) size of classes and costs; (9) faculty work load; and (10) production of graduates in other programs and schools. Motivation for change is quoted as largely supplied externally. Research needs to be done to determine the limits of growth and alternative models.

Magarrell, Jack. "State Outlook: The Economy's Recovery Eases Financial Difficulties." Chronicle of Higher Education, XIV:2, March 7, 1977.

The economy's recovery eases financial difficulties but governors say higher education is unlikely to get major budget increases. Increased spending is not indicated. Magarrell illustrates with a number of states and their plans. Overall, rises in expenditures are tied to rising costs of living.

McCoy, Marilyn and Lawrence A. Fincher. Analysis of State Financial Support of Higher Education: Pitfalls and Promises. Paper presented at the annual forum of the Association for Institutional Research, Los Angeles, 1976.

Discussed is the need to examine a number of measures of the "level" of state support of postsecondary education (e.g., in terms of a state's population, its students, and the level of state revenues). Described are factors that need to be considered as planners attempt to better understand the specific context surrounding state support decisions. The kinds of higher education institutions supported in the state, the extent to which other sources provide funding, the differential financial ability of states to furnish support, and the effects of inflation are all influences that need to be examined. Abstracted are a number of key facets of the analysis process as they affect institutional-state relations. For example, some of the tradeoffs concern the level of detail at which such analysis is conducted and how this relates to management jurisdiction; the choice between using existing data that may be less accurate but more timely and

less burdensome for institutions than the collection of new data; the appropriateness of comparative analysis, both between states and within a single state; and the responsibility of researchers in presenting analytic findings and limitations.

McFarlane, William H., et al. State Financial Measures Involving the Private Sector of Higher Education. A report to the National Council of Independent Colleges and Universities, 105 pp., 1974.

This report, commissioned by NCICU, examines financial measures in terms of constitutional limitations and programmatic details, and for evidence of impact (particularly recurrent patterns which indicate policy trends). Of note is the phrasing that government funding limitations appear not have originated from sectarian concerns, but rather sect internal divisiveness in their competition for public funds -- this has changed recently, however, with the many court cases. The argument of the maintenance of diversity in higher education supports the private sector now, along with freedom of choice, etc. Types of state aid are described within the report as well as an appendix which summarizes reports on constitutional law in most states. Individual states are assessed for impact of student aid in private colleges and universities:

1. Alaska: 59 percent of the students who receive aid indicated that it significantly influenced their choice of a private school.
2. Kansas: Approximately 10 percent of the students who received aid indicated that it significantly influenced their choice of a private school.
3. Oregon: A slight reversal in decline of financial health was detected due to five percent state assistance.
4. It was demonstrated that for a number of institutions, state aid made the difference between an operating deficit and an operating balance.

Meisinger, Richard J., Jr. State Budgeting for Higher Education: The Uses of Formulas. Berkeley: Center for Research and Development in Higher Education, University of California, 1976.

The purpose of this research effort is to determine: (1) why formulas are used in the budgetary process of public higher education, (2) what organizations play an active role in the development of the formulas, (3) what strategies and counterstrategies are adopted by the participants in the formula budgeting process for public higher education, (4) what consequences derive from the organizational strategies, and (5) what functions are performed and what dysfunctions result through the application of budgetary formulas.

This study focuses both on the historical development of budgetary formulas used in or closely related to the instructional function in California, Illinois, and Texas, and on current practices. In particular, the emphasis is on the interorganizational relationships between executive and legislative budget agencies, coordinating agencies, and institutions.

Miller, James L., Jr. State Budgeting for Higher Education: The Use of Formulas and Cost Analysis. Ann Arbor: Institute of Public Administration, University of Michigan, 228 pp., 1964.

The most significant chapter is on, "The Significance of Formulas and Cost Analysis." Validation is the theme. The same pressures that lead the colleges and universities to seek new methods to present their appropriations request will cause state officials to seek new methods to systematically analyze the requests. The advantages of use of formulas and cost analysis are summarized. Notable is equity of distribution of funds among institutions and locating key policy questions. Limitations are that numbers cannot make policy, but the maximum of information needs to be presented. Numbers are important in choosing among alternatives, and

matches resources to needs. Criteria and dangers of analysis are also discussed. The need for further research, as usual, is stressed.

Peterson, Robert G. "Environmental and Political Determinants of State Higher Education Appropriations Policies." Journal of Higher Education, 47:5, pp. 523-43, September/October 1976.

1. Impact of socioeconomic traits upon public higher education appropriations was found to be significant (although less significant than in other political influences).
2. Higher education variables showed strong associations with appropriations that demonstrated independence from effects of both the socioeconomic and political traits.
3. Significant independent impacts on senior institutions come from political variables for public higher education policy measures (i.e., inter-party competition).
4. Conclusions:
 - a. The "law of anticipated reactions" increases legislature spending.
 - b. Private colleges take the strain off public colleges.
 - c. The senior colleges are affected by very different factors than junior colleges (i.e., corporate income of area affects junior colleges positively, personal income affects senior colleges positively, as did percent of college educated).
 - d. The role of state politics needs to be better conceptualized -- methodology needs to be improved.

Purves, Ralph A. and Lyman A. Glenny. State Budgeting for Higher Education: Information Systems and Technical Analyses. Berkeley: Center for Research and Development in Higher Education, University of California, 1976.

The extent to which state agencies are implementing information systems and analytical methods for budget review are examined. Focus is on 17 states: California, Colorado, Connecticut, Florida, Hawaii, Illinois, Kansas, Michigan, Mississippi, Nebraska, New York, Pennsylvania, Tennessee, Texas, Virginia, Washington, and Wisconsin. Trends in budget information to state agencies and the bases for current concerns are reviewed. Higher education budget information categories are defined and a typology of information uses is presented. An overview is given of the trends in information and analysis activities typifying each of the state budget agencies, and the principal styles of budget review used in the states are also described. The informational content of state budget documents is delineated, followed by a discussion of the technical and political consequences of using information and analysis systems. The report concludes with a discussion of several major considerations to be weighted in setting up state-level information and analysis systems.

Russell, John Dale and James I. Doi. "Analysis of Institutional Expenditures" (a series of 12 articles). College and University Business, vol. 19, nos. 3-6, September-December 1955; vol. 20, nos. 1-6, January-June 1956; and vol. 21, nos. 1 and 2, July-August 1956.

Although 17 years have elapsed since this series of articles was published, their content represents the best available study of the techniques and problems of analyzing expenditures by institutions of higher education. The first two articles deal with general considerations underlying the analysis of expenditures. Of historical interest are the authors' examination of the need for suitable normative data. The original criticism of the data presented remain valid today; namely, gross totals rather than individual institution data are supplied and what is reported is frequently out of date. Subsequent articles deal with the

analysis of the four basic expenditure categories: instruction, library, administrative and general purpose, and plant operation and maintenance. Expenditure data collected from six New Mexico institutions are used for illustrative purposes. The understanding of expenditure analysis that can be gained from these articles should prove invaluable as an orientation for planners intending to begin formula budgeting, and useful as a refresher for current practitioners.

Schlesinger, James R. Systems Analysis and the Political Process. Santa Monica, California: The Rand Corporation, 1967.

The author is not discussing whether cost effectiveness is desirable. Instead, the real questions arise when we descend from a high level of abstraction and begin to grapple with practical issues: the quality of information bases and analyses, methodology, bias, and impact of politicized environments on analytical efforts and results. These issues are further interrelated, mechanical and organizational alike.

1. Knowledge is a form of power and most institutions exhibit an understandable reluctance to dissipate this power in the absence of compensating advantages -- ergo, information is withheld.
2. Some variables are not analyzable by current methods, subjective (not always intentional bias) analysis is a problem.
3. Systems analysis has limitations in political decision making -- the ultimate criteria is still the psychological and voting response of the electorate and pressure groups. The focus is of nature short-run.

N.B. The half-life of the public's memory is approximately three months. The appearance of effort is often more remunerative than implementation. Obviously output orientation is useless here.

Neither alternative policies nor the costs have been studied until after a decision is reached. Allocations are just not awarded rationally -- e.g., efficiently using resources to provide direct, substantive benefits.

4. The relevancy of the Department of Defense experience is discussed. It is important to note that allocative decisions cannot be based upon internally generated guidelines.
5. The encounter of the bureaucracy: (Katzenbach) "History is studded with institutions which have managed to dodge the challenge of the obvious." Obsolescence is rarely obvious. Analysis cannot bridge the gap between irreconcilable objectives. One cure is to establish efficiency as the primary goal.
6. What can systems analysis accomplish? Accept its limitations and after an educative period and its shock value and smoking out of ideologies and interests, for less resources actually will be wasted.

Schmidtlein, Frank A. and Lyman A. Glenny. State Budgeting for Higher Education: The Political Economy of the Process. Berkeley: Center for Research and Development in Higher Education, University of California, 1977.

State budget agencies, caught up in conflict over preferences, frequently use technical analyses to resolve budgetary differences in an attempt to determine objectively appropriate amounts of money for higher education. The search continues for the ultimate budget analysis system. However, if one accepts a democratic theory of choice, there are no standards or criteria for judging the value of educational services beyond those held by individuals. There is no empirical basis for maintaining that one person's preferences are better than another's. In a democratic

society, conflicts are settled by bargaining in the political arena. This bargaining is influenced by analyses of the constraints on producing services and the anticipated outputs of a given service. However, even technical considerations are often misused to gain political objectives. Greater awareness of the limits of technical analysis as a means to reduce the controversy in budget decisions will not make the life of a budget analyst any easier, but he will at least appreciate better the circumstances affecting his function and be spared unrealistic expectations.

Smith, Patricia and Cathy Henderson. A Financial Taxonomy of Institutions of Higher Education. Washington, D.C.: American Commission of Education, 1976.

This taxonomy was developed as a tool for analyzing the patterns of current fund revenues and expenditures of institutions (distinguishing influences). Expenditure patterns are important to policymakers, particularly in illustrating the case of the private colleges. The key factors which distinguish institutions from each other was revenues, not expenditures. Ergo, these factors are either directly or indirectly related to public policy. The major clusters are: tuition, endowment, revenue, annual private revenue, sponsored research, government appropriations (primarily state and local). Of note is that the private institutions varied far more in their financial profiles than those in the public sector. Tuition and private annual gift-giving is still the major source of income for both public and private sectors. The expenditures exceeded revenues by a greater margin in private institutions. Student aid expenditures were almost twice as much as student aid revenues.

Recommendations: Public policy can assist small private liberal arts colleges having great dependence on tuition and private gift-giving

by increased student aid at the federal and state levels, and increased stimuli for private gift-giving through the federal tax laws.

Van Alstyne, Carol. Progress Report on the National Debates About Financing Postsecondary Education: Ten Basic Issues. A paper for American Political Science Association Conference, August 1974.

Analyses of the issues in financing higher education have been performed chiefly by economists, or at least by analysts using economic terms: costs, cost-pricing, benefits, effectiveness, productivity, optimum allocations, trade-offs, market shares. One egregious shortcoming of such analysis is the active inference that the policy conclusions flow, more or less inexorably, from the underlying analysis. But they do not. They flow through an intermediary black box of personal and societal values which have a political dimension.

The recent history of economics as a field of study is characterized by its invasion of other disciplines. In the vanguard of the expansionist activity is a particular subset of economists who are distinguished by the intensity of their commitment to market explanations of, and solutions to, social as well as economic problems. It is time that other disciplines -- particularly political science, psychology and sociology staged a counter-invasion to illumine the extent to which the premises of economic analysis are valued-laden.

The next phase in the national debate on financing higher education should expand openly and explicitly into the political domain. We must give more attention to political motivations and processes; to questions of how effectively education interests are represented, how constituencies are formed, what the politics of educational budgeting are; and, finally, we must take a hard look at the nature of the society we have, and we must decide on the kind of society we hope to have -- all political questions.

Wynn, G. Richard. At the Crossroads: A Report on the Financial Condition of Forty-eight Liberal Arts Colleges Previously Studied. Ann Arbor: Center for the Study of Higher Education, University of Michigan, 1974.

Several years ago Hans H. Jenny and G. Richard Wynn reported on the financial condition of 48 liberal arts colleges from 1960 to 1968 in The Golden Years, which referred to the prosperous early and middle 1960's enjoyed by these colleges. The Turning Point updated their data through 1970, indicating the worsening financial condition of the 48 colleges. Jenny and Wynn were thus among those researchers who documented what some came to call a financial crisis in higher education.

This report provides data for the 48 colleges updated to 1973. And, ironically, it confirms that 1970 was indeed a turning point, but in unforeseen directions. While accelerating expenditure growth outstripped income growth, thereby producing more numerous and larger deficits from 1967 to 1970, these trends were reversed from 1971 to 1973, as expenditure growth declined dramatically and black ink replaced red.

But there is little cause for rejoicing. While an overemphasis on operating deficits might lead some to view these changes optimistically, G. Richard Wynn argues here that a new era of vulnerability may have set in for these colleges. Expenditure trends suggest that "quality distress" may replace "financial distress" as the key words of the 1970s. Surpluses are increasing, but real resource growth has come to a virtual halt at these 48 colleges. Survival may become the dominant operating principle, with quality deterioration a by-product.

These colleges collectively are "at the crossroads." Ahead may lie renewed growth, and financial and academic success; continued cost pressures that lead to widespread financial and academic bankruptcy;

or a new stability, with or without quality intact. The difficulty in predicting which scenario will dominate the years immediately ahead is the lack of accurate and timely indicators of financial and academic conditions. Until such indicators are developed, implemented, and utilized to analyze the current situation, public policy will be blind to which road these colleges are traveling, and can offer little constructive assistance.